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IN THE

Supreme Court of the United States

OCTOBER TERM, 1933.

No. 400.

CITY OF MARION, ILLINOIS, A MUNICIPAL CORPORATION; CONTINENTAL ILLINOIS BANK AND TRUST COMPANY, A CORPORATION; THE FIDELITY AND CASUALTY COMPANY OF NEW YORK, A CORPORATION, AND RAY C. CARROLL, AS TREASURER OF THE CITY OF MARION, ILLINOIS,

Petitioners,

versus

BEN SNEEDEN, AS RECEIVER OF THE CITY NATIONAL BANK OF HERRIN, ILLINOIS,

Respondent.

BRIEF OF PETITIONERS.

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Petitioners,

versus

BEN SNEEDEN, AS RECEIVER OF THE CITY NATIONAL BANK OF HERRIN, ILLINOIS,

Respondent.

BRIEF OF PETITIONERS.

To the Honorable, the Chief Justice and the Associate Justices of the Supreme Court of the United States:

Respondent, as Receiver of City National Bank of Herrin, Illinois, filed his bill in equity in the District Court of the United States for the Eastern District of Illinois, seeking to have a pledge made by that bank of certain of its assets as security for deposits of the public

funds of the City of Marion, Illinois, held invalid, and to recover the securities pledged. The case was tried upon an agreed statement of facts (R. 31) and the court dismissed the bill for want of equity. (R. 67.) On appeal, the Circuit Court of Appeals for the Seventh Circuit reversed the decree of the District Court, and (Judge Alschuler dissenting) held that respondent was entitled to the relief by him prayed. (R. 127.)

Opinions Below.

The opinion of the Circuit Court of Appeals is reported in 64 Fed. (2d) 721, and appears on pages 101-118 of the record. The dissenting opinion of Judge Alschuler is on pages 118-126 of the record. The opinion of the District Court is reported in 58 Fed. (2d) 341, and is on pages 55-62 of the record.

Jurisdiction.

The judgment of the Circuit Court of Appeals was entered April 25, 1933. (R. 127.) Petition for rehearing was denied June 1, 1933. (R. 128.) Certiorari was granted October 16, 1933 under Section 240a of the Judicial Code as amended by Section 1 of the Act of February 13, 1925. (c. 229, 43 Stat. 936, 938.)

Statement of Case.

The City of Marion, Illinois, had adopted and was operating under a statute of Illinois providing for a "Commission Form of Government."[1] Petitioner Carroll had been appointed treasurer of the city and as such was by statute required to give bond.[2] The statute further required him to

> "make his daily deposits of such sums of money as shall be received by him from all sources of revenue whatsoever, to his credit, as treasurer of said city or village, in one or more banks situated in said city or village, to be selected by the president of said council, the commissioner of accounts and finance, and the treasurer of such city or village, or by any two of them, and any such bank, before any such deposit is made therein * * * shall also execute a good and sufficient bond with sureties to be approved by the president of said council and conditioned that such bank will safely keep and account for and pay over said money * * *."[3]

Carroll applied to petitioner, The Fidelity and Casualty Company of New York, to become surety on his official bond as city treasurer. There was no bank in Marion. The Fidelity and Casualty Company agreed to execute, as surety, the official bond of Carroll as treasurer, provided Carroll would procure a bank which would give collateral security for repayment of his deposits of the public money of the City of Marion, by a pledge of some of its assets which would be satisfactory to The Fidelity and Casualty Company. Carroll, the finance commissioner of Marion, and an agent of The Fidelity and Casualty Company discussed with the

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[1] Cahill's 1931 Ill. Rev. St., Chap. 24, Par. 323-384.
[2] Id., Par. 380.
[3] Id., Par. 374.

cashier of City National Bank of Herrin the question of that bank giving security for the deposit of public money of the City of Marion by a pledge of its assets, and an arrangement was made whereby—

(a) The bank agreed to deposit with Continental Illinois Bank and Trust Company, as escrow agent, bonds belonging to the bank, to be held as security for repayment of deposits of the City of Marion's funds;

(b) Carroll and the finance commissioner agreed to make deposits of the public funds of the City of Marion in City National Bank of Herrin, which agreed that it would pay the City of Marion interest on its public moneys on deposit at the rate of 2 per cent per annum, payable monthly, on average balances in excess of $5,000; and

(c) Fidelity and Casualty Company agreed to execute, as surety, Carroll's official bond as treasurer.

In pursuance of this arrangement, on August 28, 1931, City National Bank of Herrin deposited bonds belonging to it having a par value of $23,000 with Continental Illinois Bank and Trust Company, to be held as collateral security for deposits to be made with the Herrin bank by Carroll, as treasurer of the City of Marion, of its public funds, pursuant to an escrow agreement which appears at page 10 of the record. Thereafter on the same day Carroll's bond, as treasurer, executed by The Fidelity and Casualty Company as surety, was delivered to the City of Marion (R., 34), and Carroll made his initial deposit of the public funds of the City of Marion in the Herrin bank.

When these transactions were consummated on August 28, 1931, there was no question concerning the sound financial condition of the Herrin bank. The pledge of the assets of the Herrin bank was authorized by its board of directors and was ratified by the board after

the pledge was made. The Herrin bank did not execute a bond in favor of the City of Marion conditioned for the repayment of the city's funds to be deposited with the bank.

City National Bank of Herrin failed on October 31, 1931, and respondent Sneeden was appointed receiver and thereupon took charge of the bank. At that time there was on deposit in the Herrin bank $16,430 of the public funds of the City of Marion, the deposit having been made pursuant to the arrangement hereinabove recited. On November 11, 1931, respondent Sneeden notified petitioners that he disaffirmed and repudiated the pledge made by the Herrin bank of its assets as security for the repayment of the public funds of the City of Marion on deposit in the bank, and demanded that the securities pledged be returned to him. His demand having been refused, he instituted this suit.

The questions involved are:

1. Does a national bank have general power to pledge assets as security for deposits of public moneys of states or political subdivisions thereof?

2. Does the amendment of June 25, 1930, to Section 5153 Revised Statutes, limit the power of a national bank to pledge assets as security for deposits of public moneys of a state or political subdivision thereof, to that possessed by state banks in the state in which the national bank is located?

3. Do state banks of Illinois have general power to pledge assets as security for deposits of public moneys of the state or any political subdivision thereof?

Petitioners insist that the first and third questions should be answered in the affirmative and the second in the negative and that the respondent under the facts proved in this case is not entitled to the equitable relief which he prayed in his bill.

Statutes Involved.

Federal Statutes.

By Section 8 of the National Bank Act of June 3, 1864, Chap. 106, 13 Stat. 99, 101, it was provided that national banks may

> "make contracts, * * * exercise * * * all such incidental powers as shall be necessary to carry on the business of banking by discounting and negotiating promissory notes, drafts, bills of exchange and other evidences of debt; by receiving deposits; * * *."

This provision was re-enacted without change in Sec. 5136 of the Revised Statutes and is still in force (12 U. S. C. A. Sec. 24).

By Section 45 of the same National Bank Act of June 3, 1864, 13 Stat. at p. 113, it was provided that the Secretary of the Treasury should require national banks to give

> "satisfactory security, by the deposit of United States bonds and otherwise, for the safe-keeping and prompt payment of the public money deposited with them, * * *."

This provision was also re-enacted without change in Section 5153 of the Revised Statutes and is still in force (12 U. S. C. A. Sec. 90). There was added to it by the amendatory act of June 25, 1930, Chap. 604, 46 Stat. 809, the following:

> "Any association may, upon the deposit with it of public money of a state or any political subdivision thereof, give security for the safe-keeping and prompt payment of the money so deposited, of the same kind as is authorized by the law of the State in which such association is located in the case of other banking institutions in the State."

Acts of Congress providing for the deposit of various public funds in state as well as national banks requiring the official making the deposit to take collateral security from the bank, are referred to *infra*, pp. 13, 15-18.

Illinois Constitution and Statutes.

The Illinois Constitution of 1870 (Section 5, Article XI) provides that no statute

> "authorizing or creating corporations * * * with banking powers, whether of issue, deposit or discount, nor amendments thereto"

shall become effective without a referendum.

The General Banking Act of 1887 (Laws 1887, p. 89) permitted organization of banks

> "for purposes of * * * deposit."

This provision is continued in the Banking Act of 1919 (Laws 1919, p. 224; Cahill's 1931 Ill. Rev. Stat. Chap. 16a, Par. 1). Both the 1887 and 1919 acts were approved on referendum.

Section 10 of the State Depositary Act (Laws 1919, p. 954; Cahill's 1931 Ill. Rev. Stat. Chap. 130, Par. 20) provides for the deposit of state funds in both national and state banks, and that:

> "No money in the State Treasury shall be deposited in any bank approved as a depositary under the terms of this Act until such bank shall have deposited security with the State Treasurer equal in market value to the amount of moneys deposited."

Section 11 of that act designates the type of securities to be accepted as collateral.

Provision was not made for submitting this act to a referendum.

Section 11 of the Banking Act as amended in 1929 (Laws of 1929, p. 174; Cahill's 1931 Ill. Rev. Stat.

Chapter 16a, Par. 11), approved in 1930 on referendum, provides that a receiver of a closed bank:

> "shall deposit daily all money collected by him in any state or national bank selected by the auditor, who shall require of such depository satisfactory securities or satisfactory surety bond for the safekeeping and prompt payment of the moneys so deposited."

Section 51 of the Commission Form of Municipal Government Act of 1910 (Laws 1910, p. 12; Cahill's 1931 Ill. Rev. Stat. Chapter 24, Par. 374) appears on page 3, *supra*. It was not submitted to referendum.

Summary of Argument.

The National Bank Act as originally passed conferred express power upon national banks to receive deposits and recognized that this authority carried with it the power to pledge assets as security therefor by directing the Secretary of the Treasury to require government depositaries to secure deposits of public funds. The existence of the power to secure deposits of public moneys is demonstrated by other Congressional legislation, by the uniform and long continued approval by the Comptroller of Currency of such pledges, and by numerous decisions of the Federal Courts. It is apparent from the circumstances leading up to the enactment of the 1930 amendment that that was not intended as a limitation on the powers theretofore possessed by national banks, to pledge their assets as security for deposits of public moneys of states or political subdivisions thereof. With the exception of the opinion of Judge Sparks in the present case, all other expressions of the Federal Courts as to the effect of this amendment support the petitioners' contention that this amendment did not withdraw from national banks power previously existing.

However, if after 1930 the power of a national bank to pledge its assets as security for deposits of public moneys of States or political subdivisions thereof is determined by whether or not state banks in the state in which the national bank is suituated have the power, there can be no question that national banks in Illinois still possess such power. There is no constitutional or statutory prohibition in Illinois of any kind against banks securing deposits by the pledge of assets.

The only decision of the Supreme Court of Illinois on this question, *Ward* v. *Johnson,* 95 Ill. 215, held that Illinois State Banks have the power. This decision has never been questioned in the State of Illinois, and has long been relied upon as approving of such pledges. Subsequent legislation relating to banks must be presumed to have approved of the holding in that case inasmuch as there have been no statutory enactments in any way inconsistent with it.

The Illinois Commission Form of Government Act which directs the giving of surety bonds by depositaries of city funds cannot, under the Illinois Constitution which requires acts affecting the powers of bank to be submitted to a referendum, in any manner abridge the power of Banks to make such pledges, nor was it intended by the Legislature to do so. Moreover, the Legislature has in enacting two statutes, one involving state funds, and the other relating to deposits of funds held by receivers of closed state banks, recognized and utilized the power which the Legislature must have thought Banks possessed to make such pledges. The former statute was not submitted to a referendum.

If the matter is to be determined by the weight of authority, then it is clear that state banks in Illinois possess the power. The minority view to the contrary rests upon the unsound basis that such pledges are opposed to public policy. In this connection it is significant that in at least thirty-seven states, statutes have been enacted providing that depositories of public funds may furnish pledges of securities, as distinguished from a surety bond, for the protection of various types of public funds.

In any event, if it be held that the City National Bank of Herrin did not have the power to make the pledge,

the Receiver of the Bank cannot, after the pledge has been fully executed and deposits made in reliance thereon, come into a court of equity and disaffirm the transaction consummated in good faith while the Bank was solvent.

ARGUMENT.

Point I.

National Banks Have Always Had the Power to Pledge Assets as Security for Deposits of Public Funds.

By Section 8 of the National Bank Act of June 3, 1864, Chapter 106, 13 Stat. 99, 101, re-enacted without change in Section 5136 of the Revised Statutes and still in force (12 U. S. C. A. Sec. 24), it was provided that national banks may

> "make contracts, • • • exercise • • • all such incidental powers as shall be necessary to carry on the business of banking by discounting and negotiating promissory notes, drafts, bills of exchange and other evidences of debt; by receiving deposits; • • •"

We have found no expression, prior to the enactment of this act, by courts or text-writers questioning the general power of banks to pledge assets as security for deposits of public funds.

In a case decided in 1860, in which the question was squarely raised, the court held that banks did have that power. *Smith* v. *Lansing,* 22 N. Y. 520. This court in *United States* v. *Robertson,* 5 Pet. (30 U. S.) 641 (1831), in an opinion by Chief Justice Marshall, held that a state bank with no express statutory power to pledge assets might pledge all of its assets as security for a previous deposit by the United States. The case recognized that a bank authorized to accept deposits has the inherent power to pledge its assets as security for a public deposit. Subsequently this case was approved in *Planters Bank* v. *Sharp, et al.* 6

How. (47 U. S.) 300 (1848), where the court stated (p. 323):

> "This court in *The United States* v. *Robertson*, 5 Pet. 650, has expressly recognized the authority of a bank to give bond and assignments to pay its deposit debtors. In that case 'the directors agree to pledge to the Government of the United States the entire estate of the corporation as security for the payment of the original principal of the claim' etc. (p. 648). And such a pledge or transfer was held there to be valid."

At the time, therefore, of the enactment of the National Bank Act, this court had specifically declared that banks, generally, had power to pledge their assets as security for deposits. If the power of banks to give security for deposits of public funds was then recognized by this court as inherent in or as a necessary adjunct of the power to receive deposits, the failure of Congress to limit or restrict the power granted was not only presumptive but was conclusive of the intention that such power should exist.

Congress recognized the existence of and utilized this power in the National Bank Act, as originally enacted by providing at the same time in Section 45 of the Act of June 3, 1864, 13 Stat. at page 113, re-enacted without change in Section 5153 of the Revised Statutes and still in force (12 U. S. C. A, Sec. 90), that the Secretary of the Treasury should require national banks to give

> "satisfactory security by the deposit of United States bonds and otherwise, for the safe-keeping and prompt payment of the public money deposited with them, * * *."

This provision of the law is not a grant of power to national banks, but recognizing the existence of the power, prescribes the duties of the Secretary of the Treasury relative to obtaining security for the money deposited by him. This court has held that legislative

recognition of the power or authority of a national bank is as effectual as an express declaration of the existence of the power.

In *National Bank* v. *Graham*, 100 U. S. 699, (1879) the question was whether a national bank was liable for a loss resulting from its acceptance of government bonds for deposit. The defense was made that the defendant national bank "was not authorized to receive bonds and valuables for safe-keeping." The Court stated (p. 703):

> "The Forty-sixth section of the Banking Act of 1864, re-enacted in the Revised Statutes of the United States, Sec. 5228, declares that, after the failure of a national bank to pay its circulating notes, etc., 'it shall not be lawful for the association suffering the same to pay out any of its notes, discount any notes or bills, or otherwise prosecute the business of banking except to receive and safely keep moneys belonging to it, and to deliver special deposits.' This implied clearly that a national bank, as a part of its legitimate business, may receive such 'special deposits;' *and this implication is as effectual as an express declaration of the same* thing would have been. *United States* v. *Babbit*, 1 Black, 55." (Italics ours.)

The power of solvent national banks to give, as a part of their legitimate business, security for deposits of public funds is likewise necessarily implied from the further provision in the National Bank Act forbidding all transfers of assets by an insolvent bank with a view to a preference of one creditor to another. Section 52 of the National Bank Act (Act of June 3, 1864, Chapter 106, Sec. 52, 13 Stat. 115, and the Act of March 3, 1873, Chapter 269, Sec. 2, 17 Stat. 603; R. S. Sec. 5242; 12 U. S. C. A. 91) prohibiting pledges and other transfers in contemplation of insolvency provides:

> "All transfers * * *; all assignments * * *; * * *, made after the commission of an act of in-

> solvency, or in contemplation thereof, made with the view to prevent the application of its assets in the manner prescribed by this chapter, or with the view to the preference of one creditor to another, * * *, shall be utterly null and void; * * *."

Congress further recognized the power as incidental to the right to receive deposits in the following statutes requiring custodians of public funds to obtain collateral security from the state or national banks in which such funds are deposited:

An act regulating deposits by the Comptroller of the Currency in state or national banks of receivership moneys of closed national banks (Act of June 3, 1864, Sec. 50; R. S. 5234; Chap. 106, 13 Stat. 114, as amended by Act of May 15, 1916, Chap. 121, 39 Stat. 121, 12 U. S. C. A. 192) provides:

> "* * * the Comptroller * * * shall require the depositary to deposit United States bonds or other satisfactory securities with the Treasurer of the United States for the safe-keeping and prompt payment of the money so deposited. * * *"

The "Federal Reserve Act," designating state banks and trust companies as depositaries of public moneys, (Act of Dec. 23, 1913, Chap. 6, Sec. 9, as amended by Act of May 7, 1928, Chap. 507, 45 Stat. 492; 12 U. S. C. A. 332) provides:

> "* * * The Secretary of the Treasury shall require of the banks and trust companies thus designated satisfactory security, by the deposit of United States bonds or otherwise, for the safe-keeping and prompt payment of the public money deposited with them and for the faithful performance of their duties as financial agents of the Government."

An act regulating the deposit of postal savings funds in state and national banks (Act of Aug. 24, 1912, Chap. 387, Section 1, 37 Stat. 512; Act of May 18, 1916,

Chap. 126, Section 2, 39 Stat. 159; 39 U. S. C. A. 759) provides:

> "• • • The board of trustees shall take from such banks such security in public bonds or other securities, authorized by Act of Congress or supported by the taxing power, as the board may prescribe, approve, and deem sufficient and necessary to insure the safety and prompt payment of such deposits on demand. • • •"

An act regulating deposit by Secretary of the Interior in state and national banks in Oklahoma of net receipts from sales of lands and tribal property of Indians, (Act of Mar. 3, 1911, Chap. 210, Sec. 17, 36 Stat. 1070; 25 U. S. C. A. 156) provides:

> "• • • Such depositories to be designated by him under such rules and regulations governing the rate of interest thereon, the time of deposit and withdrawal thereof, and the security therefor as he may prescribe. • • •"

An act regulating deposit by Secretary of the Interior in state and national banks of community funds of Indian tribes, (Act of May 24, 1918, Chap. 86, Sec. 28, 40 Stat. 591; 25 U. S. C. A. 162) provides:

> "• • • No tribal or individual Indian money shall be deposited in any bank until the bank shall have agreed to pay interest thereon at a reasonable rate and shall have furnished an acceptable bond or collateral security therefor, and United States bonds may be furnished as collateral security for either tribal or individual funds so deposited, in lieu of surety bonds: • • •."

An act regulating deposit by Secretary of the Treasury in state and national banks of proceeds from sales of Liberty bonds, certificates of indebtedness and war savings certificates, (Act of Sept. 24, 1917, Chap. 56, Sec. 8, 40 Stat. 291; Act of Oct. 3, 1917, Chap. 63, Sec. 214, 40 Stat. 308; Act of Apr. 4, 1918, Chap. 44, Sec. 5, 40 Stat. 504; 31 U. S. C. A. 771) provides:

> "• • • Such deposits shall bear such rate or

> rates of interest, and shall be secured in such manner, and shall be made upon and subject to such terms and conditions as the Secretary of the Treasury may from time to time prescribe. * * *"

Each of these statutes, except the "Federal Reserve Act", provides for deposits in either national or state banks. Congress cannot enlarge or restrict the powers of state banks. These statutes cannot, therefore, be regarded as evidence of intention to grant national banks additional powers; they do, however, show that Congress has, in each instance, assumed that not only national banks, but state banks as well, have general power to pledge their assets as security for deposits of public money and that the exercise of such power is merely an ordinary incident of the business of banks of deposit.[1]

Judge Sparks, in writing the majority opinion in the Circuit Court of Appeals in this case, regardless of the result which he reached, conceded that Congress in enacting these statutes, "did not intend to create additional power for national banks in the respect mentioned, but incidentally recognized the power which it thought al-

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[1] See also: The "Federal Farm Loan Act," designating Federal Land Banks and Joint Stock Loan Banks as depositaries of public money, and providing that such banks furnish satisfactory security therefor (Act of July 17, 1916, Chap. 245, Sec. 6, 39 Stat. 365; 12 U. S. C. A. 701); an Act regulating deposits of moneys of bankrupt estates providing that depositaries of such bonds shall furnish bonds as security therefor (Act of July 1, 1898, c. 541, Sec. 61; 30 Stat. 562, 11 U. S. C. A. Sec. 101); and an Act relating to the deposit of certain securities in lieu of surety bonds providing that whenever any person is required to furnish any bond under the laws of the United States such person may furnish certain securities in lieu thereof (Act of Feb. 24, 1919, c. 18, sec. 1320, 40 Stat. 1148, as amended by the Act of Nov. 23, 1921, c. 136, Sec. 1329; 42 Stat. 318; Act of June 2, 1924, c. 234, Sec. 2, 1029; 43 Stat. 253, 349; 6 U. S. C. A. Sec. 15).

ready existed under a former statute". (64 Fed. (2d) 721, 723; R. 103.)

The Comptroller of the Currency has consistently taken the position that national banks have the right to secure deposits of public money.

In *Pottorff* v. *El Paso-Hudspeth Counties Road District of Texas,* 62 Fed. (2d) 498, (C. C. A. 5, 1933) Judge Hutcheson said relative to a pledge of a National Bank securing public deposits of a Texas Road District (p. 498):

> "The bonds were made, the securities deposited, in the due and regular course of the business of the bank with the approval of the National Banking Department in accordance with the long-standing custom and practice of the Department under the rulings of the Comptroller to approve the giving by national banks of security for deposits of public funds."

In *Smith* v. *Baltimore & Ohio R. Co.* 48 Fed. (2d) 861 (affirmed, 56 Fed. (2d) 799), District Judge McVicar said (p. 867):

> "The Comptroller seems to have consistently held that national banks may pledge its assets as securities for public deposits (see Report 1657, House of Representatives, Seventy-first Congress, 2d Session, to accompany Senate Bill 486), * * *."

The uniform and long continued interpretation by the department charged with administering the Banking Act has great weight and is persuasive as to its true construction.

> *Corsicana National Bank* v. *Johnson,* 251 U. S. 68, 83 (1919).
>
> *Kern River Co.* v. *United States,* 257 U. S. 147, 154 (1921).
>
> *First National Bank of St. Louis* v. *State of Missouri,* 263 U. S. 640, 658 (1924).

FEDERAL DECISIONS.

The only decisions of the federal courts since the enactment of the National Bank Act in 1864 to which our attention has been drawn, in which the question of the power of banks to secure deposits has arisen, are the following:

Mothersead v. *U. S. F. & G. Co.* 22 Fed. (2d) 644 (C. C. A. 8th, 1927), certiorari denied 276 U. S. 637 (1928) *infra,* where a pledge of assets by an Oklahoma state bank to a surety company in connection with public funds was upheld although the state statute only authorized a pledge direct to the public official.

Parks v. *Knapp,* 29 Fed. (2d) 547 (C. C. A. 8, 1928), certiorari denied 278 U. S. 660 (1928), where transfers made in 1926 by a national bank for the benefit of sureties on a bond furnished by a depository of public funds were held invalid as illegal preferences in violation of Section 52 of the National Bank Act and also "under the law of the jurisdiction in which they were made". The bank was situated in Minnesota, and the Supreme Court of that state had adopted the minority view holding such pledges invalid. The court was clearly wrong in assuming that it was governed by the law of Minnesota. This case is perhaps one of the decisions referred to in the note p. 23, *infra,* as leading up to the enactment of the 1930 amendment to R. S. Sec. 5153.

Burrowes v. *Nimocks, County Treasurer,* 35 Fed. (2d) 152 (C. C. A. 4, 1929), where a pledge of assets by a national bank to secure funds of a county treasurer was upheld. Although the court spoke of the transaction under which the funds were delivered to the bank as one in the nature of a call loan, it was apparent that such public official had no authority to lend public moneys; furthermore, the court in its opinion relied upon *Page Trust Company* v. *Rose,* 192 N. C. 673; 135 S. E. 795,

infra, p. 46, one of the cases supporting the majority view that banks possess the general power to pledge assets as security for deposits of public moneys. In *Schumacher* v. *Eastern Bank and Trust Company,* 52 Fed. (2d) 925, 927 (C. C. A. 4, 1931) Judge Parker, who wrote the opinion in *Burrowes* v. *Nimocks,* said:

> "And this court has expressly upheld a pledge of assets by a national bank to secure a deposit of public funds. *Burrowes* v. *Nimocks, (supra).*"

Baltimore & O. R. Co. v. *Smith,* 56 Fed. (2d) 799 (C. C. A. 3, 1932, affirming 48 Fed. (2d) 861), where the court held a pledge of assets to secure a private deposit invalid but recognized that Congress had authorized national banks to pledge their assets to secure public deposits (56 Fed. (2d) at p. 802).

Texas & Pacific Ry. Co. v. *Pottorff,* 63 Fed. (2d) 1 (C. C. A. 5, 1933), now in this court on certiorari. In this case a national bank in 1931 pledged its assets in substitution for a surety bond previously given to secure a private deposit, and it was held that such a pledge was invalid and could be disaffirmed by the receiver of the bank. The court, however, considered fully the authorities relating to the power of a bank to pledge its assets to secure public deposits, and was inclined to the view that a bank possessed such power (63 Fed. (2d) at p. 3) as to public deposits but not as to private deposits (p. 4, id.).

This case was followed by the same court on a similar state of facts in *Illinois Central R. R. Co.* v. *Rawlings,* 66 Fed. (2d) 146 (1933). (A petition for certiorari is now pending in this Court.)

In *Feather* v. *School District,* decided June 7, 1933, (U. S. Dist. Ct., West Dist. of Pa., not yet reported), where a pledge was made by a national bank located in Pennsylvania, in 1931, of its assets to secure the deposit of a school district. The court, in upholding the validity

of the pledge referred to the 1930 amendment to Sec. 90 and to the Pennsylvania law, citing *Cameron* v. *Christy*, 286 Pa. 405, *infra*, p. 48.

Friend v. *School District, etc.*, decided Oct. 19, 1933 (U. S. Dist. Ct., West. Dist. of Pa., not yet reported). In this case it appeared that a pledge of two mortgages was made in 1932 by a national bank in Pennsylvania to secure the deposits of children and teachers of a certain school district. The court held that since such pledge was made to secure a private deposit it was invalid on the authority of *Baltimore and O. R. Co.* v. *Smith, supra.*

Evans v. *The New Haven Bank*, decided September 21, 1933, (U. S. District Court, District of Conn.; not yet reported). There it appeared that a State bank pledged certain bonds as collateral for deposits consisting of bankruptcy funds. In holding the pledge valid, the court pointed out that although neither by charter or statute was the Bank specifically empowered to secure deposits by pledge, such a pledge was supported by considerations of public policy which would not be applicable to private deposits.

Also see, *Pottorff* v. *El Paso-Hudspeth Counties Road District*, p. 24, *infra*, and *Fidelity & Deposit Co. of Maryland* v. *Kokrda*, p. 25, *infra*, both of which held valid pledges to secure public deposits made by national banks after the enactment of the 1930 amendment to R. S. 5153. To the same effect, see *Mays* v. *Board of County Commissioners, infra*, p. 47; and *Interstate Nat. Bank* v. *Ferguson, infra*, p. 44, as to pledges made by national banks prior to 1930.

In view of the foregoing, petitioners submit that there can be no question but that national banks possess the general power to pledge their assets as security for public deposits.

Point II.

The Amendment of June 25, 1930, to Section 5153 of the Revised Statutes Clarified and Enlarged, But Did Not Limit the Powers Previously Possessed by National Banks to Pledge Assets as Security For the Deposit of Public Moneys of States or Political Subdivisions Thereof.

As we have heretofore stated (p. 13, *supra*), by Section 45 of the National Bank Act of June 3, 1864, 13 Stat., at p. 113, it was provided that the Secretary of the Treasury should require national banks to give

> "satisfactory security, by the deposit of United States bonds and otherwise, for the safe-keeping and prompt payment of the public money deposited by them, * * *"

This provision was re-enacted without change in Section 5153 of the Revised Statutes and is still in force (12 U. S. C. A. Sec. 90). There was added to it by the amendatory act of June 25, 1930, Chap. 604, 46 Stat. 809, the following:

> "Any association may, upon the deposit with it of public money of a state or any political subdivision thereof, give security for the safekeeping and prompt payment of the money so deposited, of the same kind as is authorized by the law of the State in which such association is located in the case of other banking institutions in the State."

The Circuit Court of Appeals in this case held or assumed, without any discussion, that the 1930 amendment operated as a limitation. (64 Fed. (2d) 721, 723, R. 104.)

The amendment was not prompted by any question upon the part of either Congress or the Comptroller of the Currency as to the existence of the power, but the legislation was enacted merely for the purpose of setting at

rest a doubt that seemed to exist in the minds of some of the officers of the State of Minnesota.[1]

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[1] See, Senate Report No. 67, 71st Cong. 3d. Sess., reporting favorably upon the bill (S. 486) referring to a letter from the Attorney General of Minnesota, reading in part as follows:

> "'The United States district court for this district has held that it may not thus pledge its assets to secure private deposits and the trend of authority generally seems to be to the effect that a bank may not in any case pledge assets to secure a deposit unless authorized by law so to do. The national banks of this State have pledged with the State and various subdivisions thereof millions of dollars in Government and other bonds as security for public deposits. They are anxious to be permitted to do so, and we are willing that they should. Under the law as it now stands we may be taking a chance in accepting such pledges from the national banks, and we should like to have the chance removed by legislation in Congress which will specifically authorize such pledges by national banks.'";

See also; House Report No. 1657, 71st Congress, 2d Sess. reporting favorably upon the bill (S. 486) amending R. S. 5153, Title 12, U. S. C. A., Sec. 90, which states:

> "The purpose of the bill is to permit any national banking association to give security in the form required by State law for State banks to secure deposits of public funds of a State or any political subdivision thereof."

The following letter dated May 26, 1930, addressed to the Chairman of the House Committee on Banking and Currency by Acting Secretary of the Treasury, Seymour Lowman, is there quoted in full as follows:

> "Reference is made to S. 486, 'An act to amend Section 5153 of the Revised Statutes, as amended' which passed the Senate April 1, 1930, and which is now pending before the Committee on Banking and Currency of the House of Representatives.
>
> While the office of Comptroller of the Currency has consistently taken the position that national banks have the right to give security for the safe-keeping and prompt payment of public moneys of the State or political subdivision thereof deposited with such national banking associations, several recent decisions have thrown some doubt on this question with the result that in some States the State banks may secure the public deposits, but the officers of the State are in doubt about depositing with the national banks in the absence of any specific law by Congress on the subject. It would be extremely helpful, therefore, if it is possible for your committee to report out, and the House pass, S. 486."

In *Pottorff* v. *El Paso-Hudspeth County Road Dist. of Texas, et al.*, 62 Fed. (2d) 498, (C. C. A. 5, 1933, Certiorari denied March 20, 1933), a pledge of assets to secure road district funds made by a national bank in Texas, after the amendment, was held valid. The court with R. S. 5153 as amended called to its attention, held that the pledge was valid under the general law as well as under the law of the State of Texas.[1] The District Court Judge who tried the case (pp. 94, 95 of the Record filed in this court, Case No. 689, October Term, 1932) stated in upholding the validity of the pledge:

> "Prior to the amendment of June 25, 1930, the Comptroller of the Currency had consistently held and construed Sec. 90, 12th U. S. C. A., as permitting and authorizing national banks to put up bonds or securities for the safekeeping and prompt payment of public moneys of a state, or political subdivision thereof, deposited with such national banking association, and such position of the Comptroller had been sustained by decisions of various federal courts. Some questions seems to have arisen as to whether national banks had power as to the deposit of assets to secure public deposits equal to the power possessed by state banks, and this lead to the enactment of the amendment of June 25, 1930, to wit: Sec. 90, 12th U. S. C. A., and it is the court's holding that said amendment of June 25, 1930 was not a limitation or restriction of the powers of a national banking association as held by the courts to have existed prior to such amendment, but it was rather a broadening of the power of national banks to make deposit of assets to secure public deposits. * * *"

Judge Alschuler also held that national banks before the amendment possessed the power for which we are contending, and that such power was enlarged rather

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[1] One of the points urged in the petition for certiorari filed in this court to review the decision of the Court of Appeals which was denied, was that the amendment of June 25, 1930, to R. S. 5153 limited the power of a national bank to pledge its assets as security for the deposit of public moneys.

than restricted by the amendment. In his dissenting opinion in this case, 64 Fed. (2d) 721, 732 (R. 122), Judge Alschuler stated:

> "* * * Far from thereby withdrawing from the national bank the power it theretofore had to pledge its assets to secure deposits of public funds, the act was, in my judgment, an enlargement of its power, so that, in additional to a general right to pledge assets to secure such deposits, it thereafter had the right, notwithstanding any prior inhibition upon national banks from doing some or any of the things in that regard which might in some particular state be done by the banks thereof."

District Judge Wham, in deciding this case, 58 Fed. (2d) 341, 347, (R. 55) held that the amendment did not constitute a limitation of the powers of national banks.

In *Fidelity and Deposit Company of Maryland* v. *Kokrda*, 66 Fed. (2d) 641 (C. C. A. 10, August, 1933), the Court held valid a pledge of assets to secure County funds made by a national bank in Colorado. The Court, in denying the receiver's contention that since the pledge was not made in strict accordance with the Colorado statute it was unauthorized because of the 1930 amendment, said (page 642):

> "Section 90, *supra*, does not say a national bank may give security in the same *manner*, but that it may give security of the said *kind* as a state bank may give. *Kind* means class, character, sort, description. Webster's New International Dictionary. Had Congress intended to limit the manner of giving the security, we think it would have said, 'of the same kind and in the same manner,' or used words of equivalent import. The plain purpose of the statute was to remove any doubt of the power of national banks to give security for public deposits, and in that respect to enable them to invite public deposits on an equal footing with state banks. *Baltimore & O. R. Co.* v. *Smith* (C. C. A. 3) 56 F. (2d) 799, 802. It is our opinion that it authorizes a national bank to give the same kind of security

> for public deposits as state banks are authorized to give, in a state in which such national bank is situate, and leaves to state law the question of the procedure to be followed in the giving of such security."

It should be noted that in Illinois there is no law prescribing the type of securities to be pledged as collateral for public deposits, except that as to state funds certain kinds of securities are enumerated in Section 11 of the State Depository Act, *supra*, p. 7.

Construing the amendment of 1930 as a limitation upon the powers of national banks would necessarily have the effect of repealing Section 5153 of the Revised Statute as it previously existed. No such intent to repeal appears from the language of the amendment or the circumstances surrounding its enactment. It is fundamental, as Judge Sparks said in his opinion in the Circuit Court of Appeals, 64 Fed. (2d) 721, 728 (R. 114), that

> "* * * one statute will not be considered as repealing another statute by implication, unless the latter statute is positively repugnant to the former or a plain substitute for it. The intent to repeal must very plainly appear. *United States* v. *Claflin*, 97 U. S. 546. Such repeals will not be indulged in if there is any other reasonable construction. * * *"

We respectfully submit that the amendment of June 25, 1930, to Section 5153 of the Revised Statutes was not intended to and did not in any way derogate from the power which national banks theretofore possessed to pledge their assets as security for a deposit of public moneys belonging to a state or a political subdivision thereof.

Point III.

State Banks in Illinois Have General Power to Pledge Assets as Security for Deposits of Public Funds.

If the power of a national bank in Illinois to pledge its assets to secure public deposits is measured by the law governing state banks in Illinois there cannot be any question concerning the existence of such power.

Prior to the Illinois Constitution of 1870 there was no constitutional limitation upon the power of the Legislature to legislate concerning banks except as to banks of issue. (*People* v. *Loewenthal,* 93 Ill. 191 (1879).) The Constitution of 1870 (Sec. 5, Art. XI) provided that no statute "authorizing or creating corporations with banking powers, whether of issue, deposit or discount, nor amendments thereto" should become effective without a referendum. At the adoption of the Constitution of 1870 many banks existed under private charter and many more had been organized under the Banking Act of 1851, which, if not repealed by the Constitution, was expressly repealed by the Legislature in 1874. From that time until the adoption of the Banking Act of 1887, there was no general statute in force in Illinois providing for the organization of banks, or defining, or limiting their powers.

At the time of the adoption of the Illinois Constitution of 1870, there had been no expression by either the Illinois Legislature or its courts relative to the subject of banks pledging their assets as security for repayment of deposits. At that time, as pointed out p. 12 *supra,* this court and the Court of Appeals of New York (*Smith* v. *Lansing,* 22 N. Y. 520 (1860),) had expressly held that banks might legally pledge their assets as security for deposits.

In 1880 the Illinois Supreme Court decided the case of *Ward* v. *Johnson*, 95 Ill. 215. The Merchants, Farmers and Mechanics' Savings Bank had been organized under special charter. It operated a so-called "Investment Department" and assigned to a trustee real estate mortgages to be held as security for the repayment of amounts paid into the bank by purchasers of so-called investment certificates issued to depositors or other persons acquiring them. Upon the bank becoming insolvent, the question arose whether the securities assigned to the trustee were held primarily for the protection of certificate holders, or were available for payment of demands of depositors generally. The court, speaking by Mr. Justice Schofield, recounted the charter powers of the bank, including the power to receive money on deposit and pay interest therefor but not including the express power to pledge assets as security for deposits and then said (page 237):

> "In addition to these express powers there can be no doubt that such corporations possess, also, the implied power to borrow money. Morse on Banks and Banking, 4; *Planter's Bank* v. *Sharp*, 6 Howard (U. S.) 323; *Curtis* v. *Leavitt*, 15 N. Y. 52-3; Brice on Ultra Vires, 122 (Seward's Ed. 109).
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> *It will not therefore, be important to determine whether the certificate holders,* claiming under the trust deed, *are to be regarded as having made deposits or loans* for which their certificates were obtained, *for in the one case the requisite power is expressly given to the corporation by its charter, and in the other case it possesses the power by necessary implication.* Nor can the right of the corporation to assign or mortgage negotiable instruments which it is authorized to take be questioned. *McIntire* v. *Preston*, 5 Gilm. 48; *Planters' Bank* v. *Sharp, supra,* * * * (p. 238). The creation of the 'investment department' was not the creation of a new corporation or new agency. It was merely giving a name to a branch of business clearly within the corporate power, and indicating the system that

would be pursued in its transaction. *The corporation was authorized to contract and agree with persons desiring to make deposits or loan money as to the terms. It might execute its bond, note or certificate as evidence of the indebtedness, and secure the same by pledge or chattel mortgage, or note, securities, etc., or by real estate mortgage or trust deed, just as should be mutually agreed.* And there has been no reason suggested, and we can conceive of none, why providing a system for securing loans and deposits generally in a particular way is objectionable, when it would not be objectionable to conduct a single transaction in that way. *The business is simply that of the bank obtaining money, and so far as the public was concerned, presumably needed in its business, and securing it by a trust deed upon terms mutually satisfactory to the respective parties in interest. The name is not of the slightest consequence. The transaction itself, individually considered, is neither unusual nor extraordinary.*" (Italics ours.)

The court, in its opinion in this case, did not inadvertently fail to draw a distinction between loans and deposits but quite to the contrary deliberately refused to do so. Without recounting the history of deposit banking as Mr. Justice McKenna did in *Auten* v. *United States National Bank*, 174 U. S. 125, 141 (1899), Mr. Justice Shofield nevertheless pointed out as clearly as did Justice McKenna that the principal business of a bank is borrowing—"of obtaining money," and lending it out; and that the conduct of that business involved, as a matter of absolute necessity, the power to agree upon terms under which the capital was obtained whether the transaction be called a loan or a deposit. His conclusion was not predicated upon any special grant of power in the particular bank's charter, but upon the extent of authority inherently included in the grant of power to engage in the business of banking by receiving deposits. It was also contended by Savings depositors of the bank that

under its charter and by-laws all savings were deposited in trust, and that consequently the bank's investments of savings would also be in trust. The court rejected this contention (pp. 246-247):

> "But the investments being the general property of the bank, the board of directors might authorize them to be sold, assigned or pledged, or mortgaged in good faith, *to secure whatever loans or deposits* they might deem it advisable to obtain."

Judge Sparks, in writing the opinion of the Circuit Court of Appeals, discussed *Ward* v. *Johnson* extensively, and argued that the result reached by the court could and should have been reached by treating the transaction as a loan and not as either a deposit or a loan; stating (64 Fed. (2d) at 725, R. 108):

> "regardless of the court's statement that it was unnecessary to decide whether the money transactions between the bank and the certificate holders constituted loans or deposits, it is quite obvious that the court and counsel considered them as loans and so treated them";

and, concluding, Judge Sparks said that the Ward case could not be relied upon as an authority that Illinois had authorized its banks to pledge their assets as security for the payment of certain general deposits. Having so concluded, he said "the question therefore comes to us without helpful precedent from that state" (Illinois).

We submit that *Ward* v. *Johnson* cannot be so summarily disregarded as an authority. It is not important that that case could conceivably have been decided and an opinion written wherein the result would not have been predicated upon the alternate of two views. The fact remains that in the opinion in that case, the court said, without words of qualification, that it made no difference so far as the decision in that case was concerned

whether the fund there in question was a loan or a deposit, for in either event it was entirely within the power of the bank to pledge its assets as security therefor.

The language in the opinion in *Ward* v. *Johnson,* in so far as it treated the fund there in question as a deposit, cannot be regarded as *obiter dictum.* What this court said in *Union Pacific Railroad Co.* v. *Mason City & Fort Dodge Railroad Co.* 199 U. S. 160, 166 (1905) is apropos:

> "Of course, where there are two grounds, upon either of which the judgment of the trial court can be rested, and the appellate court sustains both, the ruling on neither is *obiter,* but each is the judgment of the court and of equal validity with the other. Whenever a question fairly arises in the course of a trial, and there is a distinct decision of that question, the ruling of the court in respect thereto can, in no just sense, be called mere dictum. *Railroad Companies* v. *Schutte,* 103 U. S. 118, in which this court said (p. 143):
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> 'It cannot be said that a case is not authority on one point because, although that point was properly presented and decided in the regular course of the consideration of the cause, something else was found in the end which disposed of the whole matter. Here the precise question was properly presented, fully argued and elaborately considered in the opinion. The decision on this question was as much a part of the judgment of the court as was that on any other of the several matters on which the case as a whole depended.' "

Subsequently, in *United States* v. *Title Insurance & Trust Co.* 265 U. S. 472, 486 (1924), this court said:

> "But it is urged that what we have described as ruled there was *obiter dictum* and should be disregarded, because the court there gave a second ground for its decision which was broad enough to sustain it independently of the first ground. The premise of the contention is right but the conclusion is wrong; for where there are two grounds, upon either of which an appellate court may rest its decision, and it adopts both, 'the ruling on neither is *obiter,* but each is the judgment of the court and of equal

validity with the other.' *Union Pacific R. R. Co.* v. *Mason City & Fort Dodge R. R. Co.* 199 U. S. 160, 166; *Railroad Companies* v. *Schutte,* 103 U. S. 118, 143."

The doctrine of *Ward* v. *Johnson* has never been departed from in Illinois; no Illinois court has ever questioned the authority of that decision. The law of the state, as declared therein, has never been altered by any constitutional or legislative provision and that case must be treated as declaring the public policy of the state.

As was held in *Zeigler* v. *Illinois Trust & Savings Bank,* 245 Ill. 180 (1910), at page 193:

> "The public policy of the State or of the nation is to be found in its constitution and its statutes, and when cases arise concerning matters upon which they are silent, then in its judicial decisions and the constant practice of the government officials * * * Courts will not look to other sources to determine the public policy of a state. As was said in *Hartford Fire Ins. Co.* v. *Chicago, Milwaukee & St. Paul Railroad Co., supra:* 'The public policy of a state or nation must be determined by its constitution, laws and judicial decisions—not by the varying opinions of laymen, lawyers, or judges as to the demands of the interests of the public.' "

Ward v. *Johnson* was decided fifty-three years ago. The courts of many states[1] have regarded it as

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Williams v. *Earhart,* 34 Arizona 565; 273 Pac. 728, 730 (1929).

First Amer. Bank & Trust Co. et al. v. *Town of Palm Beach,* 96 Fla. 247; 117 So. 900, 902 (1928).

U. S. Fidelity & Guar. Co. v. *Bassfield,* 148 Miss. 109, 114 So. 26, 31 (1927).

Melaven v. *Hunker,* 35 N. M. 408; 299 Pac. 1075, 1076 (N. M. 1931).

Page Trust Co. v. *Rose,* 192 N. C. 673; 135 S. E. 795, 797 (1926).

Cameron v. *Christy,* 286 Pa. 405; 133 Atl. 551, 553 (1926).

Grigsby v. *People's Bank,* 158 Tenn. 182; 11 S. W. (2d) 673, 676 (1928).

Pixton v. *Perry,* 72 Utah 129; 269 Pac. 144, 145 (1928).

French v. *School Dist.* 223 Mo. App. 53; 7 S. W. (2d) 415, 416 (1928).

holding that an Illinois bank has the power to pledge its assets for the repayment of deposits. Not only have the courts of other states so interpreted this decision, but Illinois banks and the customers of Illinois banks, have taken it at its plain meaning and have relied thereon in their business transactions, just as did petitioner, City of Marion. *Ward* v. *Johnson* has in effect become a rule of property and any doubt which might now be raised as to the meaning or the soundness of the decision should not be so resolved as to injuriously affect persons who in their financial dealings with banks have relied upon it.

At the time the Legislature enacted the Banking Act of 1887, it must be presumed that it was aware of the Supreme Court's statement of the law in *Ward* v. *Johnson*, and intended to adopt the construction given to the prior Act of the Legislature in *Ward* v. *Johnson*.[3] As clearly as the highest court of the State could express itself, it had been laid down as the law that an Illinois bank with the right to receive deposits had the power to pledge its assets as security therefor. By the Banking Act of 1887, which permitted organization of banks for the purposes of "discount" and "deposit," the Legislature authorized banks to be organized under its sanction for the purpose of deposit and this general grant of power without limitation as to its method of exercise must be understood to mean as the business of receiving deposits was then known and might lawfully be conducted in Illinois.

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[3] *Village of Glencoe* v. *Hurford*, 317 Ill. 203, 219, 148 N. E. 78 (1925).
People v. *I. C. R. R. Co.* 314 Ill. 373, 145 N. E. 731 (1924).
Svenson v. *Hanson*, 289 Ill. 242, 248, 124 N. E. 645 (1919).
U. S. v. *Merriam*, 263 U. S. 179 (1923).
Central Paper v. *Southwick*, 56 Fed. (2d) 593 (C. C. A 6, 1931).

The fact that the Legislature and the people conferred the power upon banks to accept deposits without limitation or qualification demonstrates that it was intended that the banks organized under the act should have the right and privilege of exercising the power to the full extent that the law of Illinois, as expounded by its Court of last resort, permitted. By authorizing banks to receive deposits, they were given power to agree with their depositors upon the terms upon which deposits should be received.

While the Banking Act of 1887 was revised in 1919, the language permitting organization of banks for "purposes of * * * deposit" has never been modified or changed, nor has there ever been any attempt to define the meaning of "deposit" or limit or qualify the manner in which the business of accepting deposits may be carried on. The Banking Act of 1887, and the amendments and revisions thereof, must be interpreted so as to accord with the existing state of the law. If it were intended that banks should not have power to pledge assets to secure deposits, or if the Legislature had believed sound public policy was opposed to the exercise of that power, a prohibition to that effect would have been written into the statute. If the manner in which the business of receiving deposits might be carried on had been particularly specified or if limitations had been placed upon the terms upon which banks might agree with their customers for acceptance of deposits then, if there had not been included the giving of security for deposits, the conclusion that the power was not conferred would be logical. But where the grant of power is as broad as expression can make it, there is no room for argument that exercise of a power is prohibited which had been judicially determined to exist as an incident of receiving deposits by an institution carrying on a general banking business.

The Illinois Legislature has assumed that Illinois

banks have power to pledge their assets as security for deposits of public funds. Section 10 of the State Depositary Act, enacted in 1919,[1] provides that

> "no money in the state treasury shall be deposited in any bank approved as a depository under the terms of this Act until such bank shall have deposited securities with the State Treasurer equal in market value to the amount of moneys deposited."

This Act does not purport to confer power upon state banks to secure the Treasurer's deposits; it provides that deposits may be made in either national or state banks without discriminating between them. In enacting this legislation the Legislature assumed that banks generally, state banks as well as national banks, had unquestioned power to comply with its provisions. It did not provide that the State Depository Act be submitted to referendum as would have been necessary under the Illinois Constitution in so far as Illinois state banks are concerned if such banks did not previously possess such power, but it is not invalid for that reason. That act is but a utilization of a power which the Legislature recognized as existing in banks generally, and a clear legislative declaration that the public policy of Illinois does not forbid its banks pledging their assets as security for deposits of public funds.

This public policy was again declared in the amendment of 1929 to Section 11 of the Banking Act, which was adopted on referendum in 1930.[2] That section, as amended, provides that the

> "receiver (of closed banks) shall deposit daily all money collected by him in any state or national bank selected by the Auditor, who shall require of such depository satisfactory securities or satisfactory surety bond for the safekeeping and prompt payment of the money so deposited."

While the amendment to Section 11 of the Banking

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[1] Laws 1919, p. 954, Cahill's 1931 Ill. Rev. Stat., Chap. 130, Par. 20.

[2] (Laws, 1919, p. 174, Cahill's 1931 Ill. Rev. Stat., Chap. 16a, Par. 11.)

Act imposed a duty upon receivers of closed state banks to obtain security for deposits of funds collected by them, there was no accompanying amendment of the provisions of Section 1 of the Banking Act, in which are enumerated the powers of banks. By the amendment of Section 11 of the Banking Act, there was again recognition, not only by the Legislature, but by the people, of the fact that the provisions of Section 1 of the General Banking Act authorizing the organization of banks "for purposes of deposit" necessarily include authority upon the part of banks to pledge their assets as security for such deposits. Section 11 of the Banking Act, as amended, likewise assumes that all banks, both state and national, have lawful power to pledge their assets as security for deposits of the character that a receiver of a closed bank would make.

Judge Sparks in his opinion in the Circuit Court of Appeals held that paragraph 374 of the Illinois Commission Form of Government Act was another obstacle which defeated appellant's right to prevail in this action. He stated that that enactment expressly set forth what an Illinois bank was authorized to do in order to secure a deposit of public funds of a city operating under the Illinois Commission Form of Government Act, and that no implication which was not clear would be permitted to strike down that express requirement. The Court further said that even if there had been a previous policy in Illinois of permitting assets to be pledged for the security of deposits, the enactment of the Commission Form of Government Act represented a change of that policy. Paragraph 374 of the Commission Form of Government Act was in no manner, or to any extent, legislation or an attempt on the part of legislature to legislate with reference to the powers of banks. The requirement that a bond with sureties be obtained affects not only deposits made in State banks, but in National Banks as well.

Under the recent (October 21, 1933) but not yet re-

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ported decision of the Supreme Court of Illinois in *People ex rel.* v. *West Englewood, etc. Bank*, in a case involving deposits of State moneys, it must be held that this requirement of the Commission Form of Government Act was merely intended to afford an additional safeguard to the public moneys, and not to affect the right of the City to enforce a pledge of securities given in lieu of a bond.

The Legislature also, by that act, obviously did not intend to, legislate with reference to the powers of national or state banks. As stated by Judge Alschuler, 64 Fed. (2d) 731, with reference to this section of the Commission Form of Government Act (pp. 731-2, R. 120):

> "These provisions prescribe the duties and direct the conduct of the treasurer and other city officers in the matter of depositing money, but in my judgment they are in no sense or degree a limiation upon the right of a bank to pledge its assets as security for deposits. If in making the deposit the treasurer does not comply with the statute, he may remain personally liable to the municipality for the safety of the deposit, but the act does not deny to banks the right further to secure the depositing municipality or its treasurer or his sureties, by pledge of assets, even though all the statutory requirements have been observed."

Similarly, in *Schornick* v. *Butler*, 185 N. E. 111 (1933), *infra*, the Court said, with reference to the Indiana Depository Law (p. 112):

> "An examination of the title and body of that act clearly discloses that it was not intended to affect the powers of banks. It merely fixed the terms and conditions upon which public officers may make deposits in banks."

Likewise in *Millard County School District* v. *State Bank*, 14 Pac. (2d) 971, (Utah 1932), *infra*, the Court stated, with reference to a statute providing that a public official required certain security as collateral therefor (p. 971):

> "In other words, the primary purpose of the stat-

ute as amended was not to restrict the authority or power of the bank in the giving of security, but more particularly to prescribe the circumstance or condition in which the officer depositing the funds may be protected; that if he takes the class or kind of collateral prescribed by the statute as amended and does that in strict compliance therewith, he shall not be personally liable or on his official bond, for a loss of moneys so deposited by him and which may be lost by reason of the failure or insolvency of the depository. *Williams* v. *Earhart*, 34 Ariz. 565, 273 P. 728, 730."

The title of the Commission Form of Government Act is "An Act to Amend an Act Entitled 'An Act to Provide for the Incorporation of Cities and Villages' approved April 10, 1872, in force July 1, 1872, and all Acts Amendatory Thereto, By Adding Thereto Article XIII."[1] Section 13 of Article IV of the Illinois Constitution of 1870 provides that "no act hereafter passed shall embrace any more than one subject and that shall be expressed in the title."

It is obvious that the purpose of the Legislature in enacting the Commission Form of Government Act was not to legislate with reference to the powers of banks and that it could not constitutionally by that legislation so entitled enlarge or abridge the powers of banks to any extent. The fact that the legislature required cities operating under the Commission Form of Government to obtain certain character of security for deposits of their public funds does not mean that the general powers of banks were thereby constricted or that all other methods of obtaining security would be illegal. If the view of the Circuit Court of Appeals is sound, then it would have been illegal for Carroll, as City Treasurer of Marion, to have deposited the city's money in any bank, as there was no bank in the city of Marion.

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[1] Cahill's 1931 Ill. Rev. Stat., Chap. 24, Par. 323, *et seq.*

Carroll as Treasurer of the City of Marion, in the absence of statute modifying his common-law liability, was an insurer of the moneys received by him by virtue of his office, and he would not have been relieved from liability by the loss of the money without his negligence or fault, whether by failure of a bank in which he might deposit such funds, or by loss by theft or robbery, if he undertook to keep them in his personal custody.[1] The Legislature, in the Commission Form of Government Act, had two purposes in view: one, the protection of public funds, and the other providing a method for limiting the liability of the Treasurer. If practical considerations were necessary to demonstrate that provision for one method of securing deposits of public funds did not operate to render any other method, otherwise lawful, illegal, the fact that Marion, a city of some 9000 inhabitants, had no bank, would serve the purpose. It has however been frequently held, in other States, that the fact that a statute requires obtaining a bond with sureties as security for deposits of public funds does not invalidate a pledge of assets as collateral security.[2]

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[1] *People* v. *Farmers State Bank*, 338 Ill. 134, 144; 170 N. E. 236 (1930).
McCormick v. *Hopkins*, 287 Ill. 66, 75; 122 N. E. 151 (1919).
People v. *McGrath*, 279 Ill. 550, 557; 117 N. E. 74 (1917). See also, excerpt from Judge Alschuler's dissenting opinion p. 37, *supra*.

[2] *McFerson* v. *National Surety Co.* 72 Colo. 482; 212 Pac. 489 (1923).
Schornick v. *Butler*, 185 N. E. 111, 112 (Ind. 1933).
Ainsworth v. *Kruger*, 89 Mont. 468; 260 Pac. 1055 (1927).
U. S. F. & G. Co. v. *Village of Bassfield*, 148 Miss. 109; 114 So. 26 (1927).
Melaven v. *Hunker*, 35 N. Mex. 408; 299 Pac. 107 (1931).
Page Trust Co. v. *Rose*, 192 N. C. 673; 135 S. E. 795 (1926).
Grigsby v. *Peoples Bank of Martin*, 158 Tenn. 182; 11 S. W. (2d) 673 (1928).

It was argued in the Circuit Court of Appeals that in view of the Illinois constitutional provision that banking legislation must be submitted to referendum, the legislature cannot, by statute not submitted to referendum, confer power upon banks to secure deposits by "recognition." We do not seek to discover the existence of the power in recognition by the legislature. We contend that the power exists and is included in the general grant of power given by the Banking Act to receive deposits for the reasons we have stated. Recognition by the legislature involves merely utilization of the power. Such recognition is particularly important both because it evidences the fact that there is no public policy in Illinois which restricts the use or exercise of the power and because it means that the legislature has as a matter of contemporaneous construction placed the stamp of its approval upon the position for which we are contending.

In the majority opinion in the Circuit Court of Appeals it was said that the question arose whether Section 51 of the Commission Form of Government Act had in any way been modified by the revision of the General Banking Act enacted on June 23, 1919, and which became effective on December 1, 1920. The revision of the General Banking Act made in 1919 in no manner changed Section 1 of the General Banking Act theretofore in effect, and which provided for the organization of banks for the purposes of discount and deposit. There is, therefore, no question presented in this case relative to modification of the Commission Form of Government Act by any other legislation relative to banks. The Commission Form of Government Act itself evidences recognition by the legislature of authority upon the part of banks to make special provision for the security of one depositor, or class of depositors, and to pledge assets for that purpose.

The legislature unquestionably recognized the existence of implied power, at least, of banks to pay a premium to a corporation duly authorized to become surety on their bonds. Nor can we imagine that the legislature was totally unaware of the usual practice of individual, as well as corporate sureties, to demand and receive indemnity for the obligations they assume. In requiring city officials to obtain surety bonds from depository banks[1] the Legislature recognized, as incidental to the right to receive city deposits the power to do those things necessary to obtain the required surety on its bond, including indemnifying the surety by the pledge of assets for the obligation it undertakes.

In this connection see *Page Trust Co.* v. *Rose*, 192 N. C. 673; 135 S. E. 795, (1926) *infra* p. 46 where the statute required banks receiving deposits of County funds, to execute a bond for the safe keeping and proper accounting of such bonds. The Bank assigned certain of its securities to sureties on its bond. The Court stated (p. 797):

> "In the instant case the Bank of Hamlet, located and doing business in Richmond county, had express authority to protect funds of said county, deposited with it by the board of commissioners, by a bond, with either person or corporate sureties. The bank has implied power, at least, to pay a reasonable premium to a corporation duly authorized to become surety on its bond. It must be held also that it has power, when required to do so, to protect personal sureties, by transfer or assignment, in good faith, of assets in value reasonably proportionate to the liability of such sureties, under the bond which is

[1] Judge Sparks was in error if he is to be understood as stating that this statutory provision was peculiar to cities under Commission Form of Government. There are similar statutory provisions relative to other cities. (Cahill's 1931 Ill. Rev. Stat. Chap. 24, Par. 100 and 287).

given to protect and thereby secure the deposits, such bond having been authorized and required by statute. The liabilities of the bank are not increased by such assignment and transfer. It has an asset in the deposit to offset its liability."

It is clear that under the decisions and statutes, a bank organized under the laws of Illinois has the power to give security for a deposit of public moneys, so that whatever effect is given to the 1930 Amendment, the decision herein of the Court of Appeals should be reversed.

Point IV.

The Inherent Power of Banks to Pledge Assets as Security For Deposits of Public Funds is Generally Recognized.

In addition to the federal decisions and the uniform and long continued interpretation by the department charged with administering the National Bank Act, the great weight of authority holds that banks inherently possess the power to pledge their assets as security for a deposit of public moneys.

The Courts in the following states have upheld the validity of pledges made to secure the deposits of public moneys and are generally (65 A. L. R. 1412) referred to as supporting the majority view:

Colorado.

In *McFerson* v. *National Surety Company*, 75 Colo. 482; 212 Pac. 489 (1923) the court upheld a pledge of collateral to indemnify sureties on bonds securing county funds. The only statute in effect at the time of the transaction called for a surety bond.

FLORIDA.

In *First American Bank and Trust Company, et al.* v. *Town of Palm Beach,* 96 Fla. 247; 117 So. 900 (1928), the court upheld a pledge of assets given in addition to a surety bond to secure the deposits of the Town of Palm Beach and those of the Commissioners of a lake District. The court held that statutes requiring certain *state* officials to demand security for deposits, constituted a legislatively established public policy that deposits of public funds should be secured by such pledges. To the same effect, see *Davis* v. *Knott,* 147 So. 276 (Fla. 1933).

INDIANA.

In *Schornick* v. *Butler, et al.,* 185 N. E. 111 (1933), the court on rehearing overruled its prior opinion in the case (172 N. E. 181) and held valid a pledge of assets to sureties on a bank's bond given in connection with the deposit of municipal funds, although the only statute authorizing the giving of collateral security to protect public funds provided that the pledge thereof be made direct to the municipality and specified a type of assets other than that pledged by the bank in that case.

IOWA.

In *Richards* v. *The Osceola Bank,* 79 Iowa 707; 45 N. W. 294 (1890), the court upheld a pledge of assets to secure County deposits. The collateral furnished was in addition to a surety bond, which was all that was called for by the Iowa Code. *Andrews* v. *Odebolt Savings Bank,* 203 Iowa 1335; 214 N. W. 559 (1929) is to the same effect.

KANSAS.

In *Interstate National Bank* v. *Ferguson,* 48 Kan. 732; 30 Pac. 237 (1892), the court held that a national bank in Kansas, under § 5136, U. S. Revised Statutes, providing that such a bank could exercise "all such incidental powers as shall be necessary to carry on the business of banking" could pledge assets as security for municipal funds.

MISSISSIPPI.

In *U. S. Fidelity & Guaranty Co.* v. *Bassfield,* 148 Miss. 109; 114 So. 26 (1929), the court upheld a pledge of assets to the surety company, to indemnify it against loss because of its acting as surety on a depository bond given in connection with the deposit of County funds. There were statutes requiring certain public officers to take collateral security in connection with the deposit of public money in designated depositories. There were other statutes providing that public money deposited in banks other than designated depositories should constitute trust funds. The Court held that the transaction in question did not come within either statute, but it concluded that the majority view was correct and that the pledge was valid as a matter of general law.

MISSOURI.

The court in *French* v. *School District,* 223 Mo. App. 53, 7 S. W. (2d) 415 (1928) and *Consolidated School District* v. *Citizens Savings Bank,* 223 Mo. App. 940, 21 S. W. (2d) 781 (1929) upheld pledges of assets to secure the deposits of school district funds. The only statute referred to by the court authorizing the giv-

ing of collateral to secure public moneys related solely to County funds.

MONTANA.

The court in *Ainsworth* v. *Kruger,* 89 Mont. 468; 260 Pac. 1055 (1927), held that a pledge of assets to a bank director, to indemnify him against loss as surety for the bank, on bonds given to protect County deposits, was valid.

NEW MEXICO.

In *Melaven* v. *Hunker,* 35 N. M. 408; 299 Pac. 1075 (1931), the court upheld a pledge of assets to sureties to indemnify them against loss as sureties on bonds given to secure County deposits despite the fact that the particular assets pledged were not of the character prescribed by statute.

NEW YORK.

In *Smith* v. *Lansing,* 22 N. Y. 520 (1860) *supra, Application of Broderick,* 252 N. Y. Supp. 68; 140 Miss. Rep. 861 (1931), and *In re Bank of Spencerport,* 255 N. Y. Supp. 482; 143 Miss. Rep. 196 (1932), the courts have upheld pledges of assets given as security for public moneys,—in the *Smith* case for State funds, in the *Broderick* case for school district funds, and in the *Spencerport* case for town funds. In the *Spencerport* case the statute prescribing the manner of depositing town funds merely called for a surety bond. In the *Broderick* case the statute called for "security". The decision in the *Smith* case was based entirely upon the court's understanding of the general law and no statute was referred to.

In *State Bank of Commerce* v. *Stone,* 261 N. Y. 175, 184 N. E. 750 (1933), the Court of Appeals, confining itself to private deposits, held that while a bank had no power to pledge assets for such deposits, the receiver could not reclaim the assets pledged, without repaying the deposit thereby secured.

NORTH CAROLINA.

The courts in *Page Trust Co.* v. *Rose,* 192 N. C. 673; 135 S. E. 795 (1926) and in *Richmond County* v. *Page Trust Co.,* 195 N. C. 595; 142 S. E. 786 (1928), upheld pledges made by the same bank to different individuals, to indemnify them as sureties on the bank's bond given in connection with the deposit of County funds. The North Carolina statutes required the public officials to take a surety bond, but did not provide for the taking or the giving of collateral security in lieu thereof.

OHIO.

In *Snider* v. *Fulton,* 44 Ohio App. 238, 148 N. E. 839 (1932), the court held a pledge given to the State Superintendent of Banks as security for the deposit by him of funds of a closed bank, valid. In so holding, the court pointed out that while Ohio statutes requiring officials to take collateral security in connection with deposits of state, county and municipal funds were not applicable, they did disclose a public policy in favor of protecting the particular fund in question.

OKLAHOMA.

In *Mays* v. *Board of County Commissioners of Creek County*, 23 Pac. (2nd) 664 (Okl. 1933), in 1927 a national bank in Oklahoma pledged certain of its assets to secure county funds. In upholding the validity of the pledge, the court first held that a national bank possessed the general power to pledge its assets as security for public deposits, referring to various Federal cases, including the decision of the District Court in our case, 58 Fed. (2nd) 341, and rejected the cases announcing the minority rule, stating (p. 668) that they were not

> "in any way persuasive * * * for the reason that we are governed by the rules declared by the Federal courts in so far as they announce a rule relative to national banks and we are controlled by our statute in so far as State banks are concerned."

The court then referred to the various Oklahoma statutes relating to deposits of public funds and, after considering the effect of various amendments thereto, concluded that pledges of assets could be made to secure county funds, and rejected with brief comment the contention that the pledge was invalid because of non-compliance with certain formalities provided for in the Oklahoma statutes.

With reference to the Oklahoma statutes the court cited *Maryland Casualty Co.* v. *Board of County Commissioners*, 128 Okla. 58, 260 Pac. 1112 (Nov. 1927) to the effect that a statute prohibiting pledges securing deposits had been repealed, in so far as it related to county deposits, by a subsequently enacted statute specifically dealing with county funds. In that case, the court held that the latter statute authorizing the pledging of assets in lieu of or in addition to a surety bond did not author-

ize a pledge of assets in addition to a surety bond where the amount of the bond exceeded the amount on deposit by the county and accordingly that the surety company on the bond could not avail itself of such pledge. The court did not have occasion to pass on the general question as to the power of banks to pledge their assets as security for public deposits.

In *Mothershead* v. *U. S. F. & G. Co.* 22 Fed. (2d) 664, C. C. A. 8th (Oct. 1927), certiorari denied, 276 U. S. 637 (1928), it appeared that numerous Oklahoma State banks pledged certain of their assets to a surety company to indemnify it against loss on account of its liability as surety on various public depository bonds of such banks. The Bank Commissioner in charge of the liquidation of the depository banks contended that such pledges were *ultra vires*. The court rejected this contention and pointed out that under the Oklahoma law the bank could have pledged these assets directly to the depositor in lieu of a surety bond and therefore that a pledge made directly to the surety was valid.

PENNSYLVANIA.

In *Cameron* v. *Christy,* 286 Pa. 405; 133 Atl. 551 (1926), the court upheld a pledge of assets to secure the deposits of county funds although there was no statute providing therefor. The court relied upon its earlier decision in *Ahl* v. *Rhoads,* 84 Pa. 319 (1877) and commented upon the fact that the practice of giving pledges of that character was common in Pennsylvania.

TENNESSEE.

In *Grigsby* v. *Peoples Bank,* 158 Tenn. 182, 11 S. W. (2nd) 673, (1929), a State bank's pledge of assets to indemnify the sureties on a bond given in connection with the deposit of State and County funds was held valid. The only applicable statute was one which provided that any bank might become a public depository of money of the state by executing a bond to secure such funds. The Court held that this evinced a legislative intent to require security for state funds and stating that "the record presents a legal question which is determinative and may thus be stated: Can a state bank, engaged in the general banking business, pledge its assets to secure general depositors," answered the question in the affirmative.

UTAH.

In *Pixton* v. *Perry,* 72 Utah 129, 269 Pac. 144 (1928) a state bank pledged certain of its assets to secure a deposit of county funds. It appeared that at that time there was in force a statute which prohibited preferences to any depositor by pledging the bank's assets as collateral security and there was another statute which provided with reference to public funds that the public officer having custody thereof take from the depository "collateral security" or a bond. It was contended by the State Bank Commissioner in charge of the liquidation of the bank that under such statutes the pledge of assets was invalid, and that only a bond could be furnished as security. In rejecting this contention the court held that the latter statute was controlling and, after

referring to the cases representing the so-called majority and minority view with reference to the power of a bank to pledge its assets to secure public deposits, stated (p. 145) "we find it unnecessary to determine which line in our opinion states the better rule or which is better grounded on legal principles."

In *Millard County School District* v. *State Bank,* 14 Pac. (2d) 967 (Utah, 1932) a State bank between May 11 and May 15, 1929 pledged certain of its assets consisting in part of notes and mortgages to secure a deposit of school district funds. It appeared that on May 14, 1929, an amendment was passed to the Act relating to deposits of public funds which provided that only United States, State and municipal bonds could be accepted as collateral security. The court first held that the pledge of assets occurred before this amendment went into effect and therefore that under the decision of *Pixton* v. *Perry, supra,* the pledge of assets would be valid. The court further held that even if the transaction took place after May 14, 1929, the pledge would be valid even though not consisting of the type of assets referred to in the 1929 amendment and that in any event the Bank Commissioner, as well as the bank, would be estopped from asserting the invalidity of the pledge.[1]

The decisions in the states of Arizona and Nebraska have not consistently aligned themselves with either the majority or minority view, but we comment on them for purposes of completeness.

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[1]Subsequent to these decisions, the Legislature prohibited pledges to secure deposits with certain exceptions (Laws of Utah, 1933, c. 47, p. 84 *et seq.*).

ARIZONA.

Although the court in *Williams* v. *Hall*, 30 Ariz. 581; 249 Pac. 755 (1926) and *Williams* v. *Earhart*, 34 Ariz. 565; 272 Pac. 728 (1929), upheld pledges of assets to secure the deposits of public moneys, the same court in the later case of *Button* v. *Sanguinetti*, 11 Pac. (2d) 1085, attempted to explain its previous holdings in the *Hall* and *Earhart* cases upon the estoppel theory.

NEBRASKA.

In *Bliss* v. *Mason*, 121 Neb. 484, 237 N. W. 581, (1931), a State Bank pledged certain of its assets consisting in part of corporate bonds and foreign Government bonds to sureties on a county depository bond. At the time the transaction took place there was a statute which provided for the giving of security as collateral for county deposits, but did not include the type of securities above mentioned. The court in upholding the validity of the pledge followed what it termed the majority view, holding that the bank was not limited to a pledge consisting of the type of securities enumerated in the statute, and also that such a pledge could be made directly to the sureties as well as to the county.

In *Bliss* v. *Pathfinder Irr. Dist.*, 122 Neb. 203, 240 N. W. 291, (1932), a state bank pledged its assets directly to an irrigation district to secure a deposit made by the latter. The court in holding the pledge invalid first pointed out that an irrigation district was not a municipal corporation and its deposits were not covered by the statutes providing for the pledging of assets of a bank to secure certain public deposits. The court expressly limited the holding of *Bliss* v. *Mason* to county funds, cited approvingly the cases upholding the minority view.

The courts in the following states have held that banks in the absence of statute do not have the power to pledge assets as security for deposits of public moneys, and represent what has been referred to as the "minority view."

ARKANSAS.

In *Arkansas-Louisiana Highway Improvement District* v. *Taylor,* 177 Ark. 440; 6 S. W. (2d) 533 (1928) and in *Arkansas County Road Improvement District* v. *Taylor,* 185 Ark. 293; 47 S. W. (2d) 27 (1932), the court held the pledges invalid to secure deposits of highway and School District funds. There was a statute calling for the giving of certain types of collateral security in lieu of a surety bond. The collateral was not of the specified type and the court held that the power to pledge assets should not be extended beyond that expressly authorized by the legislature.

CALIFORNIA.

In *Wood* v. *Imperial Irrigation District,* 216 Calif. 748, 17 Pac. (2d) 128, (1932), a State bank in 1925 pledged certain of its assets as collateral security to a deposit by an irrigation district. It appeared that under the laws then in force such a pledge could have been made as collateral to deposits of the State, County, municipalities or other political subdivisions, and that in 1927 a statute had been enacted which permitted the pledge of collateral to secure the deposits of irrigation districts. The court first held that the irrigation district was not a "municipal corporation" or "political subdivision" within the meaning of the constitutional provision referred to above, and also that the 1927 Act would not be applicable to a transaction which had taken

place previous thereto. The Court then based its decision on the ground that in the absence of a statutory provision expressly approving the pledge "the general policy of the law will not sanction it," relying on the decisions representing the minority view. The court also held that the State Superintendent of Banks, as trustee in charge of the liquidation of the bank, was not estopped to assert the illegality of the pledge.

KENTUCKY.

In *Commercial Bank and Trust Company* v. *Citizens Trust and Guaranty Co.*, 153 Ky. 566; 156 S. W. 160 (1913), a pledge of assets by a state bank to a surety company to indemnify it against loss for acting as surety on the bank's bond to the County Treasurer, was held invalid. The court decided that the banking laws did not grant the power expressly, and that it could not be implied. The court found that for many years state officials had invariably construed Ky. St., Sec. 4693, requiring security from depositories for state funds, and Sections 411 and 2903 *id.*, requiring security from depositories for certain court and city funds as calling for individual or corporate sureties only and not for pledges of assets. There was no statute calling for security of any kind from depositories of County funds.

In 1918, however, a statute was enacted permitting state banks to pledge their assets as collateral security for deposits of United States funds (Ky. Statutes, Carroll's 1930 Ed., Sec. 579), and in 1932, a similar statute was enacted relative to vario s types of public funds (Ky. Acts, 1932, c. 13, p. 46).

MINNESOTA.

In *Farmers and Merchants State Bank* v. *Consolidated School District No.* 3, 174 Minn. 278, 219 N. W. 163 (1928), a pledge to secure School District funds was held invalid. There was a statute providing that qualified depositories could pledge certain specified collateral security in lieu of a surety bond. The court found that the bank had not qualified as a depository and the securities pledged were not of the type authorized by the statute. The court held that the power to pledge assets, except where expressly authorized by statute, was contrary to the public policy of the state, and that Chapter 257 G. L. 1927, prohibiting them, enacted subsequent to the transaction involved, merely expressed the public policy of the state as it had previously existed.

NORTH DAKOTA.

In *Divide County* v. *Baird,* 55 N. D. 45; 212 N. W. 236 (1926), a pledge to secure County funds was held invalid. The only statute involved required the County Treasurer to take a personal bond, or in lieu thereof a surety bond. There were no statutes referred to authorizing the giving of collateral security to secure any public funds.

TEXAS.

In *Foster* v. *City of Longview,* 26 S. W. (2d) 1059 (Commission of Appeals 1930) reversing 11 S. W. (2d) 217 (Court of Civil Appeals), a state bank pledged certain of its assets to secure a deposit of city funds, and at that time there was no statute providing for the pledging of any type of collateral to secure such deposits. The court, in holding such pledge invalid, stated that in

the absence of any statutory authority, such pledge was forbidden by public policy, and illegal. In *Austin* v. *Lamar County,* 26 S. W. (2d) 1062 (1930) reversing 11 S. W. (2d) 553, (Court of Civil Appeals), the same court on the same day held invalid a pledge made by a state bank to secure a deposit of county funds, because the assets pledged were not of the type specifically provided for in a statute then in force relative to county funds. The court, in following *Foster* v. *City of Longview, supra,* held that such pledges were against the public policy of the state since not expressly authorized by statute.

These courts, following the minority view, which refused to sustain the validity of pledges of assets as security for public funds, reached their decisions by holding that in the absence of express statutory authorization, banks have no such power and that statutes authorizing the pledging of assets of a certain kind in lieu of surety bonds are exclusive and permit of no other type of collateral. In the last analysis, however, the opinions in these cases demonstrate that they are predicated upon the view that such pledges are opposed to public policy; that they perpetrate a type of constructive fraud upon unsecured depositors in favoring a limited number of secured depositors as opposed to the greater number of general depositors, who, because of the secrecy usually existing in such pledges, have no means of knowing the extent of the bank's reported assets that are so pledged. That no basis for such view exists, was clearly pointed out by Circuit Judge Alschuler in his dissenting opinion in 64 Fed. (2d) 721, 731 (R. 118) where he said:

> "It is pointed out, in support of such a public policy of the state, that ordinarily there is secrecy

in such pledges of which the general public has no notice, and that depositors not so secured would usually have no means of knowing how much of the bank's reported assets are so segregated.

It seems to me that the vice is not with the pledging of the assets, but with the laws and regulations concerning reports and advertisements of banks. I fully agree that banks should be required to make frequent public reports of their condition, and that in such reports it should be specifically disclosed what part of the reported assets is so pledged. To my mind it is vicious practice to permit banks to advertise their 'resources' at an amount inclusive of their total deposits, without requiring that at the same time, and quite as prominently, there be stated the liabilities to which the resources are subject.

It is also pointed out that such pledging of a bank's assets may, in case of the bank's threatened disaster, enable certain depositors to be favored as against others. This, of course, would bring into the picture collusion and probably fraud, which would be dealt with when it appears, but which is not involved here, where concededly there was no suggestion of circumvention or favoritsm, and where, at the time of the pledge, the bank was solvent."

Courts in upholding pledges to secure public funds have expressed themselves in like manner.

In *Grigsby* v. *Peoples Bank,* 158 Tenn. 182; 11 S. W. (2d) 673 (1929) *supra,* the court said:

"Our statutes, requiring periodical published statements of the condition of banks, makes it a serious offense to publish a false statement. Shannon's Annotated Code, Chaps. 2104—2104a4. A true statement would include 'secured deposits,' and it is the duty of the banking department of the state to require this in the form which it is authorized to provide for such statements. If this is done, we are unable to see how any hardship can result to unsecured depositors or stockholders further than would result where the bank borrowed a fund and pledged its assets as security."

In *First American Bank & Trust Co. et al.* v. *Town of Palm Beach,* 96 Fla. 247; 117 So. 900, (1928) *supra,* the court stated:

> "It has been contended that, to hold that the pledging of securities to pretect deposits in state banks would be unfair to other depositors who are unsecured, because the financial reports of banks show as a part of the assets securities which are pledged to protect deposits, without indication that such securities are so pledged. If this contention is true, it may be easily obviated by the state comptroller requiring financial statements and reports of state banks to show what amounts of the assets of the bank is pledged as security for deposits."

An examination of the statutes of the different states in the Union demonstrates that legislative bodies generally, recognize that the public welfare demands that public funds deposited in banks be adequately protected, and have utilized the power of banks to pledge their assets as security for public funds.

In at least thirty-seven states there are statutes providing that public officials may take a pledge of securities from banks as distinguished from a surety bond for the protection of various types of public funds.[1]

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[1] *Alamaba,* Code 1928, § 893 (State Funds); *Arizona,* Laws 1923, c. 45, Laws 1927, c. 71 (Public Funds Generally); *Arkansas,* Acts 1931, Act 212, p. 684 (State Funds), Acts 1927, Act 182, p. 634 (Funds of various Improvement Districts); *California,* Statutes and Amendments 1923, p. 21 (State Funds), p. 25 id. (County and Municipal Funds), Statutes 1927, p. 188 (Irrigation District Funds); *Colorado,* Laws 1927, p. 206 (County Funds); *Florida,* Compiled General Laws 1927, § 6079 (Public Funds Generally), §§ 173, 174 id. (State Funds); *Georgia,* Laws 1931, p. 120 (State Funds); *Idaho,* Code, Ann. (1932), Title 55, p. 74 *et seq.* (Public Funds Generally), Title 65, §§ 2625, 2626, id. (State Funds); *Illinois,* Laws 1919, p. 954

As stated by this Court in *Twin City Co.* v. *Harding Glass Co.*, 283 U. S. 353, 357 (1931):

> "Primarily it is for the lawmakers to determine the public policy of the state."

In view of such extensive legislation providing for

(State Funds), Laws 1929, p. 174 (Funds of State Bank Receiver); *Indiana*, Burns Ann. Statutes 1926, § 10321 (Deposits of Sinking Fund Commissioners), § 12622 id., as amended, Acts 1929, c. 132, p. 437 (Public Funds Generally); *Kansas*, Laws 1927, c. 89, § 1 (State, Postal Savings and Public Funds Generally); *Kentucky*, Acts 1932, c. 13, p. 46, amending § 579 Kentucky Statutes, Carroll's 1930 Ed. (United States and Public Funds Generally); *Louisiana*, General Statutes (Dart) § 6639 (State and Public Funds Generally); *Maryland*, Ann. Code (Bagby, Art. 90, § 9) (State Funds), Laws 1933, p. 1092 (Funds held by bank commissioner as receiver of closed bank; Laws 1931, p. 1093, empowering state banks to deposit securities for the purpose of securing deposits of the United States, State, County, City, Town, and other political subdivisions of the State of Maryland; *Michigan*, Compiled Laws 1929, § 348 (State Funds), Public Acts 1931, No. 22, p. 33, as amended, Public Acts 1932, No. 31, p. 47 (Public Funds Generally); *Minnesota*, Laws 1933, c. 41 (Public Funds Generally); Laws 1925, p. 173 (State Funds), Laws 1925, c. 202 (Funds of Cities Operating Under Home Rule); *Mississippi*, Code 1930 Ann., c. 105, § 4326 (State Funds), § 4346 id. (County Funds), § 4357 id. (Drainage District Funds), § 4358 id. (Municipal Funds); *Missouri*, Laws 1931, p. 378 (State Funds), Laws 1927, p. 324 (Funds of Cities of the First Class), Rev. Statutes 1919, § 9585 (County Funds); *Montana*, Laws 1909, c. 129, § 1 (State Funds), Rev. Codes Supp. (1923-27), § 4767 (County, City and Town Funds); *Nebraska*, Laws 1933, c. 147, p. 564 (State Funds), Compiled Statutes 1929, c. 77, § 2508 (County Funds), 1931, c. 28, p. 115 (Funds of Cities of the First Class); *Nevada*, Compiled Laws, (Hillyer, 1929) § 7032 (State and County Funds); *New Mexico*, Laws 1933, c. 175, § 6 (Public Funds Generally, Including State); *New York*, Laws 1931, c. 45, as amended Laws 1932, c. 97, (County Funds), Cahill's Cons. Laws (1930), c. 15, § 254 (4) (School Funds), c. 57, § 10 id. (State Funds), c. 57, § 11 id. (funds of charitable and benevolent institutions supported by the State), c. 65, § 89 (20) id. (Village Funds), also see Greater New York Charter, § 196, as amended Laws 1917, c. 617; *North Carolina*, Laws 1925, c. 128, § 2 (State Funds); *Ohio*, 1 Page's Ann. Ohio Gen. Code §§ 330-3, as amended, 4 Page's Ann. Ohio, Gen. Code, p. 12 (State Funds),

pledges by banks to secure public deposits, it seems unreasonable to contend that a practice so widely sanctioned is contrary to public policy.

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1 Page's Ann. Ohio Gen. Code, § 2732 (County Funds), § 4295 id. (City and Village Funds); § 7605 id. (School Funds); *Oklahoma*, Statutes 1931, Sec. 5416 (State Funds), § 5459 id. (School Funds), § 7428 id. (County Funds); *Oregon*, Laws 1925, c. 207, § 90, p. 307, as amended, Laws 1933, c. 227, Sec. 7, p. 316 (Public Funds Generally, Including State, United States and Postal Savings Funds); *Pennsylvania*, Laws 1929, p. 865 (City Funds), Laws 1906, p. 45 (State Funds); *South Carolina*, Special acts have been passed from time to time, providing with specific reference to deposits of certain counties, that the county treasurer require the depository bank to deposit either a surety bond or certain types of security as collateral for the deposit, see, *e.g.*, Acts 1930, Act 1039, p. 887, Acts 1927, Act 47, p. 86, Acts 1926, Act 514, p. 952; *South Dakota*, Compiled Laws 1929, § 6875 (State Funds), § 6883 id., as amended, Session Laws 1929, p. 100 (County Funds), Compiled Laws 1929, § 6344, as amended, Session Laws 1929, p. 217, Session Laws 1931, p. 154, as amended, Sessions Laws 1933, p. 90 (School Funds); *Tennessee*, Public Acts 1931, c. 104, p. 361-365 (State Funds); *Texas*, Rev. Civil Statutes 1925, Art. 2429, p. 664, as amended, General Laws 1933, c. 240, p. 840, c. 244, p. 54 (State Funds), Art. 2547, p. 670 Rev. Civil Statutes 1925 (County Deposits), Laws 1929, c. 61, p. 160, expressly provides that a bank may pledge its assets as collateral security for certain public deposits; *Virginia*, Code (1930) Ann. § 2158 (State Funds); *Washington*, Remington's Compiled Statutes (1922), § 5549 (State Funds), §§ 5569, 5572 id. (City Funds), §5563 id. (County Funds), also see, Sess. Laws 1931, c. 87, p. 255 *et seq.* increasing the type of securities available as collateral under the above sections; *West Virginia*, Acts of Legislature, Extra Sess. 1932, c. 8, p. 13 (County Funds); *Wisconsin*, Statutes 1929, c. 60, § 29 (25) (Town Funds), c. 20, § 35 (38) id. Village Funds), c. 62, § 13 (c) id. (State Funds); *Wyoming*, Laws 1907, c. 30, § 8, as amended, Laws 1909, c. 94 (State Funds), Laws 1907, c. 30, § 20 (County, City, Town and School Funds), also see, Session Laws 1925, c. 83, p. 86, and c. 157, p. 220 id.

Point V.

The Receiver Should Not Under Any Circumstances Have the Relief He Seeks.

The Receiver's suit is addressed to the equity side of the Court, and he seeks equitable relief. If the facts proved do not show that equitably he is entitled to the relief prayed, then his bill should be dismissed. He had no statutory authority to disaffirm the pledge which was made; the pledge was not made in contemplation of insolvency, and consequently the provisions of Section 52 of the National Bank Act, *supra,* prohibiting pledges and other transfers in contemplation of insolvency, are not applicable.

Pledges of assets by national banks as security for public deposits of states, or other political subdivisions thereof, are not prohibited by the National Bank Act; they are not *malum in se,* nor contrary to the public policy of the federal government. National banks have general power to secure such deposits; the most that can be claimed is that there is a limitation upon the exercise of the power by certain banks or in certain states. It cannot be contended, therefore, that this pledge was unlawful *per se;* the most that can be claimed is that the bank in question exercised a general power conferred upon it in an improper manner. There is neither rule of law nor reason for requiring that the public suffer loss of security for its funds under these circumstances. The recent decision of the New York Court of Appeals in *State Bank of Commerce* v. *Stone,* 261 N. Y. 175, 184 N. E. 750 (1933) *supra,* supports this contention. To the same effect, see *Millard County School District* v. *State Bank,* 14 Pac. (2nd) 967, 973 (Utah, 1932) *supra.*

The transactions of which the Receiver complains were fully executed at the time of his appointment; there has been no attempt to prove that any general creditor of the

bank has actually been injured or will suffer damage by reason of the bank's bonds having been pledged in order to obtain deposit of the city's funds. There is no contention that the value of the bonds pledged was excessive in proportion to the amount of city funds deposited. Of course, if the pledge had not been made, the proceeds of the bonds would, presumptively, be available in their entirety for distribution to general creditors. But, if the pledge had not been made, the bank's currency would, on the other hand, be diminished to the extent of the amount of the city's funds on deposit, and any gain to general creditors, on the one hand, would be offset by equal loss on the other. The bank itself could not have recovered its bonds without having repaid the city the amount of funds it had on deposit. If the bank had repaid the city and recovered its bonds, the amount of the bank's assets standing as security for other depositors would not have been increased one penny's worth. Other depositors, or the Comptroller of the Currency of the bank, could not, prior to its insolvency, have compelled or obtained recovery of the bonds pledged without repayment of the city's deposit. To permit the recovery, therefore, by the Receiver of the bonds pledged, without repayment of the deposit liability secured thereby, is to create in the Receiver a right, for the benefit of general creditors, which did not exist either in their favor or in favor of the bank prior to his appointment, and for which no equitable basis exists. To condemn as void a transaction, fully executed and not at the time it was entered into injurious to the bank or its depositors, and to permit the Receiver to retain the benefit of the transaction and disclaim its liability, does not satisfy that sense of justice which is equity. Congress has not intended that such a result shall be accomplished. It has declared void only such transfers or assignments of a bank's assets, after the commision of an act of insolvency, or in contempla-

tion thereof, as are made with a view to the preference of one creditor to another; by as strong implication as can be gathered from language used, the recovery of assets, transferred in ordinary course of business, for value received, and without contemplation of insolvency, is prohibited. If the deposits made by Carroll in the Herrin bank be regarded as made in violation of the provisions of the Illinois Commission Form of Government Act, then, in accordance with the usual rule, the bank became a trustee *ex maleficio* because of its receiving the deposit, and, in equity, the bonds pledged as security for the deposit should be regarded as impressed with a trust in favor of the city.

The Receiver did not in this case bring himself within the provisions of Section 52 of the National Bank Act by showing that the pledge resulted in a preference; he did not make out a case for relief appealing to the conscience of the Court, or requiring the interposition of a court of equity, and his bill should, therefore, be dismissed.

Petitioners respectfully submit that for the reasons above stated the judgment of the Circuit Court of Appeals herein should be reversed, and the decree of the District Court dismissing the bill be affirmed.

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